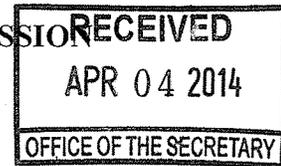


UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-15015

In the Matter of

RALPH CALABRO;
JASON KONNER; and
DIMITRIOS KOUTSOUBOS

Respondents.

**DIVISION OF ENFORCEMENT'S BRIEF IN RESPONSE TO
CALABRO'S OPENING BRIEF IN SUPPORT OF HIS PETITION FOR REVIEW**

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The Division of Enforcement (“Division”) respectfully submits this Post-Hearing Brief in response to Respondent Ralph Calabro’s (“Calabro”) “Opening Brief In Support of Petition For Review” filed on March 5, 2014. This brief is timely submitted pursuant to the Securities and Exchange Commission’s (“Commission”) Order dated January 24, 2014.

Calabro’s appeal asserts that in the Initial Decision dated November 8, 2013, the Administrative Law Judge (“ALJ”) applied incorrect standards as to *de facto control* and as to excessive trading in the JP Turner & Co., LLC (“JP Turner”) account of client [REDACTED] [REDACTED] for whom Calabro served as registered representative. Calabro also contends that, despite the conclusions of the ALJ, no churning occurred in Williams’ JP Turner account, Calabro committed no fraud, and that even if the account was churned, the ALJ’s decision should nevertheless be modified to eliminate any monetary obligations that the ALJ ordered Calabro to pay. The Initial Decision from which Calabro’s appeal is taken, followed a 17 day hearing held from January 28 – February 20, 2013.

I. INTRODUCTION

A. Broad Overview of Case Brought By the Division Against JP Turner Registered Representatives And Supervisory Executive Vice-President

The case that is before the Commission on appeal pursuant to the petitions for review filed by Respondents Calabro, Jason Konner (“Konner”) and Dimitrious Koutsoubos (“Koutsoubos”), is a substantially narrowed case from that originally authorized by the Commission and then brought and tried by the Division. The Order Instituting Proceedings (“OIP”) in this matter is dated September 10, 2013. Approximately four months thereafter, this

¹ [REDACTED] is a former JP Turner client, whom the ALJ concluded had his firm brokerage account churned by Calabro. (Initial Decision, pp. 107-110). John Williams was a Brooklyn, NY branch office compliance officer for JP Turner who testified at the hearing related to the conduct of Konner and Koutsoubos, but whom the ALJ found decisively to be not credible, as a witness. (Initial Decision, pp. 87-92; 105; 117).

case was tried before ALJ Cameron Elliot over a four week period in January and February 2013. The litigated case that the Commission authorized involved seven clients of JP Turner, including the three clients of Calabro, Konner and Koutsoubos, respectively, that are the bases for their petitions for review of the Initial Decision.²

The OIP alleged and the Division offered proof at trial to establish that at various times between January 2008 and December 2009, three registered representatives at JP Turner – Respondents Calabro, Konner and Koutsoubos – churned the accounts of several customers. In each instance, Respondents Calabro, Konner and Koutsoubos enticed investors with little or no experience in high-risk investments to trust them, and thereafter, convinced them to invest aggressively and trade often without ever adequately disclosing the risks involved. During the relevant period, the turnover rate for each of the investors at issue exceeded levels presumptive of churning. Consequently, these customers collectively lost approximately \$2.7 million and paid approximately \$845,000 in commissions, fees, and margin interest to JP Turner which, in turn, paid a portion of the commissions and fees to the three registered representatives.

In addition, the OIP alleged and the Division offered proof at trial that Michael Bresner (“Bresner”), who during the relevant time was the firm’s head of supervision, Executive Vice President and a senior member of management, also failed reasonably to supervise Konner and Koutsoubos, who generated sufficiently high commissions for some of their churned customers

² In addition to this litigated case, the Commission also instituted settled proceedings against JP Turner and its President. *In the Matter of JP Turner & Company, LLC and William L. Mello*, AP File No. 3-15014 (September 10, 2012). The settled case related to the firm’s and President Mello’s failure to establish reasonable policies and procedures that would have detected excessive trading in customer accounts at JP Turner. The firm was censured and Mello was suspended from association in a supervisory capacity with any broker, dealer or investment adviser for a period of five months. JP Turner was ordered to pay disgorgement of \$200,000 (that portion of commissions received from churned accounts which the firm retained), prejudgment interest of \$16,051, and a civil money penalty in the amount of \$200,000. The firm’s president was ordered to pay a civil money penalty in the amount of \$45,000. Paragraph 15 of that Order alleged that one of the registered representatives at issue was ranked as the firm’s top revenue generator in 2008 and 2009, when he generated more than \$3,000,000 during that period. As established by relevant evidence at trial in the litigated case which is now before the Commission, that registered representative was Calabro, whose appeal is now before the Commission. (T. 296-297; DOE Exs. 202, 203).

that the firm's procedures required Bresner to personally review the underlying trading. Despite numerous red flags, Bresner took no meaningful action to investigate or prevent the churning.

The Division sought cease and desist orders and industry bars against Calabro, Konner and Koutsoubos for violations of Section 17(a) of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act") for this fraudulent conduct. The Division also sought disgorgement along with prejudgment interest. The disgorgement sought by the Division was based upon the retained portions of the sales commissions that Calabro, Konner and Koutsoubos received as payment for the trades during the churn periods. The Division further sought civil penalties against Calabro, Konner and Koutsoubos pursuant to Section 21B of the Exchange Act and Section 9 of the Investment Company Act. In his Initial Decision, the ALJ granted full relief against Calabro for his churning in the JP Turner account of [REDACTED], but found Calabro did not churn the JP Turner accounts of [REDACTED] or [REDACTED].³

The Division also sought and obtained a supervisory bar against Bresner pursuant to Section 15(b)(6) of the Exchange Act, which incorporates by reference Section 15(b)(4)(E) of the Exchange Act and pursuant to Section 203(f) of the Investment Advisers' Act ("Advisers Act"), for failing reasonably to supervise Konner and Koutsoubos, who each willfully violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The Division also sought and obtained against Bresner a civil penalty pursuant to Section 203 of the Advisers Act.

³ The ALJ also granted full relief against Konner for his churning in the JP Turner account of [REDACTED], but found Konner did not churn the JP Turner account of [REDACTED]. The ALJ further granted the Division full relief against Koutsoubos for his churning in the JP Turner account of [REDACTED], but found that Koutsoubos did not churn the JP Turner account of [REDACTED].

In essence, with regard to Calabro, the Initial Decision found for the Division on one churn victim account holder at JP Turner, [REDACTED], but found *against* the Division on two other alleged client victims.⁴ Despite Calabro's predictable but erroneous arguments that the ALJ applied *incorrect standards* to conclude that Calabro *de facto* controlled [REDACTED]' JP Turner account and that the trading in [REDACTED]'s account was excessive, the ALJ's conclusion was based largely upon the credibility determinations as to various JP Turner clients, the registered representative respondents who served them, the churning and supervisory experts proffered by the Division, and the credibility determinations that the ALJ found as to other related witnesses at trial.

As evidenced by the Initial Decision finding *against* the Division on four of seven allegedly churned JP Turner clients, the ALJ carefully evaluated the credibility of each witness in reaching his conclusion that Calabro churned the [REDACTED] account. Indeed, in the extensive 125 page Initial Decision, the ALJ painstakingly summarized the relevant evidence in unusual detail, made the detailed credibility determinations as to the essential witnesses, and further made the appropriate findings of fact and conclusions of law to reach his narrowed opinion, and to impose sanctions against the Respondents. The Initial Decision was plainly no rubber stamp of the Division's case.

B. The ALJ's Credibility Determinations In the Initial Decision Make Up The Substantial Issues Before the Commission On Appeal

The Commission conventionally extends substantial deference to the credibility determination of the ALJ as the initial fact finder, and it should do so in this case. *See Leslie A. Arouh*, Exchange Act Rel. No. 50889 at n.40, 2004 WL 2964652 (Dec. 20, 2004) ("As we have stated previously, the credibility determination of an initial fact finder is entitled to considerable

⁴ The Initial Decision also finds for the Division with respect to one investor serviced by the other respondents who were registered representatives, but finds against the Division with regard to the other customers.

weight and deference because it is based on hearing the witnesses' testimony and observing their demeanor"), citing, *Daniel Joseph Alderman*, 52 S.E.C. 366, 368 (1995), *aff'd*, 104 F.3d 285 (9th Cir. 1997); *Jonathan Garrett Ornstein*, 51 S.E.C. 135, 137 (1992). As recently reiterated by the Commission relating to reviews of credibility, "[a]lthough we grant 'considerable weight and deference' to credibility determinations of law judges and other initial factfinders, we judge those determinations against the weight of the evidence." *David F. Bandimere*, Securities Act Release No. 9512, Exchange Act Release No. 71333, 2014 SEC LEXIS 158 at n. 12.

Calabro's appellate brief seeks to avoid this deferential standard by couching the arguments in terms of legal error. For example, Calabro contends that the "ALJ applied an incorrect standard" on the issue of *de facto* control, when he concluded that Calabro had the *de facto* control of ██████████' JP Turner account. (Calabro Brief, pp. 7-13). The thrust of the argument is that ██████████ allegedly had sufficient intelligence and understanding to evaluate Calabro's recommendations and to reject anything he thought was unsuitable. Calabro also argues that the ALJ applied an incorrect standard and erred in concluding that excessive trading occurred in ██████████' JP Turner account. (Calabro Brief, pp. 14-25). The thrust of his argument on this point was that the churn period on the ██████████ account coincides with a volatile period in the market, and the latter somehow excuses, or changes the standard for excessive trading. Both arguments are misleading in that they seek to avoid the credibility determinations and conclusions that the ALJ made regarding ██████████' true investment objectives and who actually controlled the account.

For the reasons set forth below, Calabro's arguments depend upon overturning the credibility determinations of the ALJ. The ALJ essentially found that customer Williams was a credible witness and that Calabro was not credible on critical points. Williams' testimony that he had conservative investment objectives was corroborated by the minimal trading activity in his

single prior, non-JP Turner, brokerage account. The ALJ also concluded that Louis Dempsey, the Division's expert on excessive trading (and indeed the only expert related to churning who took the witness stand at trial) was indeed credible in his calculations on turnover and cost-equity ratios in the [REDACTED] account. As Calabro produced no expert or other witness to rebut Dempsey's calculations which established an equity turnover of 8 and a cost equity rate of 22.9% on an annualized basis during the relevant period of the churn in [REDACTED] account (December 1, 2008 through November 30, 2009), Calabro is left with only extraneous arguments related to the volatility of the market in that period. Those arguments were previously raised by Calabro, and were rejected (as to [REDACTED]) by the ALJ in his Initial Decision. The credibility findings of the ALJ are entitled to deference in this proceeding, and the credibility determinations support the ALJ's conclusions on the elements of churning in the [REDACTED] account.

II. THE ALJ'S RELEVANT CREDIBILITY FINDINGS ARE VALID, AND SUPPORTED BY EVIDENCE IN THE RECORD

A. Relevant Evidence in the Trial Transcript From [REDACTED]

[REDACTED], a 76 year-old, long retired college professor, lives in Claremont, California. [T. 1390-93]⁵ For thirty years, [REDACTED] taught statistics, quantitative management, introduction to business, production management and production related courses to students at Cal Poly University. [T. 1399-1400] [REDACTED] testified that he does not consider himself to be a sophisticated investor; that he then had no active brokerage accounts, and has only had three accounts in his life. [T. 1402-03; 1406] [REDACTED] never took any courses related to stock market investing, and never taught any finance or investment courses. [T. 1399-1400] While he did subscribe to the Wall Street Journal for a mere two-year period, [REDACTED] did not

⁵ Exhibits from the trial will be identified by their exhibit number ("DOE Ex. ___" for the Division's exhibits; "C-___" for Respondent Calabro's exhibits; "JK-___" for Respondent Konner's exhibits; "DK-___" for Respondent Koutsoubos's exhibits; and "B-___" for Respondent Bresner's exhibits). The transcript of the trial will be identified as "T. ___."

typically read investment-related periodicals or watch investment-related television shows, and he did not know what a chat board is. [T. 1411] ████████ does not own a computer, does not know how to turn on his wife's computer, and has never had an e-mail account in his name. [T. 1446-47]

Prior to opening his account with JP Turner, ████████ had one brokerage account at Smith Barney that he opened in 1991 and closed in 2008. The account consisted of common stocks, mutual funds and municipal bonds. In marked contrast to the heavy trading volume in his JP Turner account, ████████ continued to hold 95% of the stocks that were purchased in the Smith Barney account until he closed it. [T. 1406-09.] ████████ never bought options or traded on margin in the Smith Barney account, and he relied on his registered representative to select the stocks that were purchased. [T. 1409-10.] ████████' trading in that account included stock in Disney, JP Morgan, Chase, Chevron, Exxon, Pfizer and other blue chip stocks to be held long term. [T. 1409]. ████████ opened another brokerage account at Newbridge Securities in 2009, the third of three brokerage accounts that he has had in his life. [T. 1403] By the time of trial, ████████' Newbridge account had been closed. The Smith Barney, JP Turner, and Newbridge brokerage accounts constituted ████████' entire investment experience in stocks.

In the fall of 2007, ████████ received a recommendation from his friend of more than 40 years, ████████, to speak with Calabro about possibly investing with Calabro. [T. 1414] ████████' Smith Barney broker had retired and he was felt the account was being neglected. [T. 1408-09; 1414] ████████ indicated at the time he liked Calabro and recommended him to ████████ based on Calabro's claims to be able to invest successfully in an up or down market. [T. 1414-15] After a short conversation with Calabro, ████████ opened an account with JP Turner in October 2007 and began funding the account in late November or early December 2007. [T. 1414-16; DOE Ex. 43] ████████ closed his Smith Barney account when he opened his

JP Turner account and used the funds from his Smith Barney account to fund his JP Turner account. [T. 1406-07] [REDACTED] initially funded the account with \$200,000. Over the course of the next several months, [REDACTED] ultimately transferred a total of \$1.7 million to the account. [T. 1417-18]

[REDACTED] signed the account opening application on October 31, 2007.⁶ [DOE Ex. 43] Much of the information on the application, including all of the information in the Account Owner profile, was added to the form after [REDACTED] signed it, and much of it was wrong. [T. 1436-42] The form indicates [REDACTED]' primary investment objective was speculation, but [REDACTED] did not intend to speculate in the account. [T. 1442-43] In addition, [REDACTED]' risk tolerance was not aggressive, as marked on the form, but instead was conservative or moderate. [T. 1444] [REDACTED]' annual income – a subject he never discussed with Calabro – was \$100,000, not the \$150,000 reflected on the application. [T. 1437-38] Further, [REDACTED]' net worth was not \$3 million, as the form reflected. [T. 1438-39] Calabro never discussed the form or the investment objectives marked on it with [REDACTED]. [T. 1443-44] Calabro was fully aware, however, that [REDACTED] was retired at the time the account was opened. [T. 1421-23] In fact, [REDACTED] had retired from his 30 year teaching career *in 1995*, more than 12 years before he opened his JP Turner account. [T. 1392-93]

[REDACTED]' goal in his JP Turner account was to protect the money he currently had and to make a fair return on the money invested. [T. at 1430-31] Calabro never asked questions about [REDACTED]' true investment objectives. [REDACTED] insisted that he was not a risky or speculative

⁶ The relevant exhibits relating to the establishment and maintenance of [REDACTED]'s account at JP Turner include DOE Ex. 43 (account application of JPK 755982), DOE Ex. 8 (JPT statements for [REDACTED]' account for Churn Period December 2008 through November 2009), DOE Ex. 44 (handwritten notes of [REDACTED] to Calabro re his account), DOE Ex. 45 (Active Account Suitability Questionnaire and Supplement dated 3/18/2009), DOE Ex. 46 (Supp. Application for margin privileges) and DOE Ex. 47 (completed JPT Options Suitability Questionnaire and Option Trading Agreement).

investor. [T. 1431-33] ██████ testified that if he had filled out the investment objectives on the account opening form, he would have listed preservation of capital, income and capital appreciation. [T. 1443] Calabro told ██████ that he could make him money in an up economy or a down economy. [T. 1426] Calabro also told ██████ he would take care of him as he had taken care of his friend, ██████. Calabro explained to ██████s that he engaged in short sales, which was a new and foreign concept to ██████s. Specifically, Calabro explained that in a down economy, you sell stock now, which you later buy back at a reduced price and make money. ██████ testified that he did not fully understand what short selling meant, and still did not understand it at the time of trial, but trusted Calabro and went along with Calabro's recommendations. [T. 1426; 1428-29]

Between late 2007 and early 2008, ██████ and Calabro spoke about once a week, with Calabro normally making the calls. [T. at 1420-23] ██████ never recommended stock transactions to Calabro, and did no investment research of his own. [T. 1452; 1456-57] Calabro told ██████ which securities he was buying, or going to buy, and what stocks he was shorting. ██████ relied on Calabro's recommendations 100% of the time and always accepted Calabro's recommendations. [T. 1449-50; 1456] ██████ never discussed or challenged Calabro's recommendations because he did not feel he had the background or knowledge to do so. [T. 1450] ██████ believed that Calabro was looking out for ██████' best interest. [T. at 1458-59] Although ██████s did not give Calabro discretionary authority, Calabro made trades for ██████ without seeking preauthorization. [T. 1450-51] During the churn period, (December 1, 2008 through November 30, 2009) Calabro executed 271 trades in ██████' account. [T. at 1506-08.]

██████ received an Active Account Suitability Questionnaire (AASQ) and Supplement in March 2009. [DOE. Ex. 45] He signed the form in blank and returned it. None of the

information appearing on the form was written by ██████, and virtually all of it is untrue or inaccurate. [T. 1478, 1479-85] In particular, the investment objectives marked included short-term trading, speculation, trading profits and growth are not accurate – ██████' true investment objectives at the time were safety of principal and income. [T. 1481-82] Other account documents sent to ██████ were similarly signed in blank and later filled out by Calabro containing inaccurate information and untrue investment objectives. [DOE Ex. 46; T. 1490-95; DOE Ex. 47; 1495-1500]

Moreover, in ██████' account, virtually all of the relevant documents which falsely list him as a speculative investor with an aggressive risk tolerance, and/or falsely inflate his Estimated Annual Income, Net Worth and Liquid Net Worth are in Ralph Calabro's handwriting. If not in his handwriting, Calabro admits that he populated the typed forms with the substantive information. [T. 4228-4229 (DOE Ex. 10--██████' Active Account Suitability Questionnaire); T. 4230 (DOE Ex. 11--██████' JPT account application); T. 4253 (DOE Ex. 43--██████' JPT account application); T. 4256 (DOE Ex. 45-46--██████' AASQ and application for Margin Account Privileges); T. 4257 (DOE 47—JPT Options Trading Agreement for ██████)].

██████ insists convincingly that he and Calabro never discussed the substantive information that the forms contain.⁷ [T. 1430-32, 1435, 1477-1480, 1485].

When read as a whole, one cannot conclude that ██████' assertion that Calabro had him sign blank or partially completed forms for his JP Turner account is untrue, as Calabro argues. In fact, ██████ is consistent in his testimony that he did not see all of the questions or all of the responses on the JP Turner forms that he signed for Calabro. [T. 1440-41, 1517-18].

⁷ It should not be overlooked that while Calabro had largely claimed he sent no blank forms to ██████ and/or ██████ Calabro ultimately admitted upon cross-examination in his case in chief that he had in the past sent out blank forms for signature. [T. 4243, 4245].

Specifically, *some* of the information was typically included on the forms [REDACTED] signed, while other information was missing and filled in later. [T. 1437-1440, 1441-45, 1478, 1497-98, 1517-18, 1519, 1608-09, 1610]. For example, on the Active Account Suitability Questionnaire (“AASQ”) that Calabro asked [REDACTED] to sign, the only information filled in on that form was [REDACTED]’ name, age and marital status. [T. 1643-44]. All of the information was later filled in which falsely listed [REDACTED] as a speculative investor, and falsely stated his stock trades averaged \$400,000. [T. 1643-44; DOE Ex. 45].

[REDACTED] lost \$1.3 Million in his JP Turner account over approximately a 1 year period. [T. 1434] [REDACTED] had approximately 65% of his net worth in his JP Turner account. [T. 1508] When [REDACTED] confronted Calabro as the losses in his account began to mount, Calabro told him that the account would turn around. [T. 1434-35; 1452-53] Although Calabro had never mentioned commissions to [REDACTED], [REDACTED] confronted Calabro about the commissions he was paying. In response, Calabro told [REDACTED] that active trading was necessary because of the volatility of the economy. [T. 1461-62; 1504] This was the first time that Calabro discussed active trading with [REDACTED]. [T. 1461-62]

The Commission should note the circumstances as to how [REDACTED] came to be aware of active trading in his JP Turner account. [REDACTED] had never actively traded in any account in his life. He first discussed the active trading in his JP Turner account when he confronted Calabro about concerns he had over the commissions he was paying. [T. 1460-62]. Calabro’s explanation was to tell [REDACTED] that now that the economy was volatile, active trading was necessary to “keep his head above water” in the account. [T. 1461-62]. Williams explained that he initiated the discussion with Calabro on the amount of commissions being generated, because he had not been used to paying lots of commissions that he came to find he was paying to JP Turner and Calabro. That was how [REDACTED] learned his JP Turner account was an actively

traded account—and not because Calabro had vetted with him the issue of an actively traded account.

B. Relevant Evidence In the Trial Transcript From Ralph Calabro

Respondent Ralph Christopher Calabro, age 39 at the time of the trial, resides in Matawan, New Jersey. [T. 79] Calabro graduated from Xaverian High School in Brooklyn in 1991. [T. 91-92] He attended Kingsborough Community College in Brooklyn for less than two years, and took some courses at the Fashion Institute of Technology in New York, but holds no secondary degree. [T. 92] Calabro has held a Series 7 securities license that allows him to recommend stocks, bonds and options to brokerage clients for 18 years. [T. 92-93] He also holds a Series 63 “Blue Sky” license and a Series 24 license that permits him to be a brokerage principal/supervisor. Calabro previously faced a churning claim in an arbitration that was settled for cash in 2008. [T. 88-89]

At the time of his trial testimony, Calabro was working as a registered representative for National Securities. [T. 105] Prior to that firm, Calabro worked as a registered representative for JP Turner from early 2004 through January 2011.⁸ [T. 104-05] While working at JP Turner, Calabro oversaw customer accounts, made recommendations to customers regarding their accounts, and acted as a securities principal. [T. 114-15] Calabro worked in the Parlin, NJ office of JP Turner, which was an Office of Supervisory Jurisdiction (“OSJ”) with Calabro serving as the principal/supervisor. [T. 121] While employed by JP Turner, Calabro was responsible for originating his own business, which he did using cold calls and referrals. [T. 136-37]

During his time at JP Turner, Calabro claimed that he sought out as customers those investors who were active traders and risk takers. [T. 143] He claimed to have looked for

⁸ In the decade before joining JP Turner, Calabro worked at approximately ten (10) other securities industry firms; none for longer than 2 years, 4 months. [T. 98-103; DOE Ex. 1]

individuals (preferably accredited investors) wanting to invest money they could afford to lose into an account set up with speculative objectives. [T. 139-40; 143-46] Calabro claimed that because of his approach to the market, he also acknowledged the importance of his clients' understanding of, and ability to withstand, risk. [T. 182] Calabro professed to have asked questions of potential customers to confirm that his investment style was appropriate for them during the cold calling process, [T. 175-85] including asking specifically about their investment objectives and risk tolerance. [T. 190-195] He claimed to have often used charts to explain his trading strategy – which supposedly was based on Keynesian theory as expressed over a “parabola cycle” – to customers. [T. 160-61; 172-73] Calabro claims that he did not look for investors seeking a steady rate of return on a large portion of their net worth, did not recommend CDs or mutual funds, and did no financial planning for customers. [T. 142-44]

During 2008 and 2009, Calabro admitted that he personally filled out the account opening documents for more than 50% of his new customers. [T. 194] During the same period, he managed accounts for approximately 70 JP Turner brokerage customers. [T. 185] Most of those customers received JP Turner's AASQ and Supplement forms, which typically meant the accounts had been flagged at Level 2 or higher on the firm's Active Account Review System (“AARS”). [T. 236] Despite claiming that he generally sought authorization from customers before executing trades in their accounts, Calabro could not affirmatively state that he *always* received pre-authorization from the customers at issue in this case. [T. 229-31]

Regarding compensation, Calabro did not receive a salary while working at JP Turner, but instead received a percentage of commissions and fees generated by his customers' accounts. At JP Turner, customers were typically charged a commission ranging from 1% to 5% per trade on both purchases and sales. [T. 134-35; 218-219] Under his contract with JP Turner, Calabro retained 85% of all commissions generated by his customers' accounts up to \$25,000/month, and

he kept 90% of all commissions that exceeded \$25,000. [T. 219-20] Calabro also kept \$9 of a \$39 ticket charge imposed by JP Turner on every transaction, and he received 1/10 of 1% on an annual basis of the average daily balance of his customers' margin trading accounts. [T. 220-21] In 2008, Calabro was the top commission-earner among registered representatives at JP Turner, making approximately \$2 million. [T. 296; DOE Ex. 202] In 2009, he was the third highest-ranked commission-earner in the firm, making \$1.7 million. [T. 297; DOE Ex. 203]

C. Relevant Evidence From Louis Dempsey, The Expert On Excessive Trading In ██████████' JP Turner Account

Dempsey's review of the activity in the ██████████ account and the monthly statements revealed that during the period from December 2008 through November 2009, Calabro engaged in trading patterns consistent with churning by executing over 122 sales transactions totaling \$8,588,124.41 and over 149 purchase transactions totaling \$11,015,161.13. These trades resulted in losses in the account of approximately \$1,026,546 and generated commissions and fees to JP Turner of approximately \$297,515. Calabro's aggressive trading in this account resulted in an annualized equity turnover of 8 times on an annualized basis and a cost equity factor of 22.9%. Dempsey confirmed that virtually all of the transactions in the ██████████ account were marked solicited, indicating Calabro's control over the trading in the account. Based on Calabro's testimony during the investigation that his payout ratio was 95% of gross commissions, Calabro earned commissions of over \$282,000 as a result of the trading activity in the ██████████ account. [DOE Ex. 155, pg. 15-16 The ██████████' Account Trading Activity, ¶27]

D. The ALJ's Credibility Determinations As to ██████████, Calabro And The Expert Dempsey

As between JP Turner client ██████████ and registered representative Calabro (both of whom testified extensively at trial in this matter) the ALJ found ██████████ to be a generally

credible witness, noting that his “demeanor, particularly the tone of his voice, bolstered his credibility.” (Initial Decision p. 107). The ALJ further concluded that “[redacted]’ testimony regarding his investment experience, his investment objectives, and his dealings with Calabro were especially credible.” *Id.* In comparing the two witnesses, the ALJ concluded “[b]y contrast, Calabro’s testimony was inconsistent and sometimes extremely confusing on numerous points.” *Id.* at 107.

On the issue of whether [redacted]’ FINRA claim against JP Turner and Calabro gave [redacted] a motive to be untruthful, as Calabro had argued, the ALJ found:

Moreover, even assuming that [redacted]’ pending FINRA arbitration gives him a motive to be untruthful, Calabro’s motive is even stronger, because he is faced with potential arbitration awards pertaining to [redacted] and [redacted] as well. As between [redacted] and Calabro, I generally find [redacted] to be the more credible witness. Initial Decision, p. 107

Simply put, the ALJ rationally concluded that if [redacted] had a financial motivation that may affect the veracity of his testimony, Calabro had a much greater financial motivation because he was being sued in FINRA cases by multiple JP Turner clients, not just

[redacted].

E. The Elements of Churning And The ALJ’s Credibility Determinations As To Those Elements In [redacted]’ JP Turner Account

Section 17(a) of the Securities Act prohibits using the mails or instruments of interstate commerce in the offer or sale of securities to (1) employ any device, scheme, or artifice to defraud; (2) use false statements or omissions of material fact to obtain money or property; or (3) engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser of securities. *In re Dale E. Frey*, Admin. Proc. File No. 3-10310, 2003 SEC LEXIS 306, at *45 (Feb. 5, 2003) (initial decision). Section 10(b) of the Exchange Act and Rule 10b-5 make it unlawful for any person, directly or indirectly, in

connection with the purchase or sale of any security to (1) employ any device, scheme, or artifice to defraud; (2) make any untrue statement or omission of a material fact; or (3) engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person. Id.

To state a claim under the antifraud provisions, the Division must show that the defendants acted with scienter. See *Rogers v. Sterling Foster & Co.*, 222 F. Supp. 2d. 216, 268-9 (E.D.N.Y. 2002); Frey, 2003 SEC LEXIS 306, at *45. Scienter is defined as “a mental state embracing intent to deceive, manipulate, or defraud.” *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). Recklessness satisfies the scienter requirement in a civil enforcement action under Section 10(b) and Rule 10b-5. See *SEC v. Falbo*, Civil Action No. 92 Civ. 6836, 1998 U.S. Dist. LEXIS 16020, at *2 (S.D.N.Y. 1998); *SEC v. McNulty*, 137 F.3d 732, 737 (2d Cir. 1998) (stands for the proposition that willful ignorance satisfies scienter). Proof of scienter can be inferred from circumstantial evidence. See *Herman & MacLean v. Huddleston*, 459 U.S. 375, 391 (1983).

Churning violates the antifraud provisions. See *Mihara v. Dean Witter & Co., Inc.*, 619 F.2d 814, 820-21 (9th Cir. 1980); *Newburger, Loeb & Co. Inc. v. Gross*, 563 F.2d 1057, 1069 (2d Cir. 1977), aff'd in part, rev'd in part, 611 F. 2d. 423 (2d Cir. 1979), cert. denied, 434 U.S. 1035 (1978). *Sandra K. Simpson*, Exchange Act Release No. 45923 (May 14, 2002) (Commission opinion). Churning occurs “when a broker engages in excessive trading in disregard of the customer’s investment objectives for the purpose of generating commission business.” *Rolf v. Blyth, Eastman, Dillon & Co.*, 424 F. Supp. 1021, 1039-40 (S.D.N.Y. 1977), aff'd, 570 F.2d 38 (2d Cir. 1978), cert. denied, 439 U.S. 1039 (1978). To establish a claim of churning, the Division must prove (1) trading in the account that is excessive in light of the investor’s investment objectives, (2) explicit or de facto control over that trading by the broker, and (3)

scienter on the part of the broker, which is established either by evidence of intent to defraud or by evidence of willful and reckless disregard of the customer's interests. See In re Al Rizek, Exchange Act Release No. 41725, 1999 SEC LEXIS 1585, at *17 (Aug. 11, 1999) (Commission opinion)), aff'd, *Rizek v. SEC*, 215 F.3d 157 (1st Cir. 2000); *Miley v. Oppenheimer & Co.*, 637 F.2d 318, 324 (5th Cir. 1981), reh'g denied, 642 F.2d 1210 (5th Cir. 1981); *Moran v. Kidder Peabody & Co.*, 609 F. Supp. 661, 666 (S.D.N.Y. 1985); *Rush v. Oppenheimer & Co.*, 592 F. Supp. 1108, 1112 (S.D.N.Y. 1984), vacated, 596 F. Supp. 1529 (S.D.N.Y. 1984), rev'd, 779 F.2d 885 (2d Cir. 1985). "Churning, in and of itself, may be a deceptive and manipulative device under section 10(b), the scienter required by section 10(b) being implicit in the nature of the conduct." *Armstrong v. McAlpin*, 699 F.2d 79, 91 (2d Cir. 1983).

1) The ALJ's Finding That Calabro Exercised De Facto Control of ██████' Account Is Based On Credibility Determinations, And Should Be Affirmed

In concluding that Calabro exercised *de facto* control of ██████' account, the ALJ relied on the credibility of ██████' testimony. Specifically, the ALJ opined:

Based on ██████' credible testimony, I conclude that he never made securities recommendations and that Calabro traded without his knowledge, and without discretionary authority. Tr. 1451. Accordingly, even if ██████ was comfortable with rejecting Calabro's trade recommendations, Calabro usurped control of his account by engaging in unauthorized trading, thereby making it impossible for ██████ to evaluate and reject unsuitable recommendations. Additionally, I find ██████' testimony that Calabro called him just to tell him what trades he was making in ██████ account, his testimony that he accepted what Calabro told him as correct and he did not try to change Calabro's mind, and his testimony that he never took it upon himself to research Calabro's recommendations, credible. [Initial Decision, p. 108].

The ALJ also found that Calabro's "confusing" and "self-contradictory" explanations for his frequent trades "adversely affect[ed] his credibility." (Initial Decision, p. 15, FN 5). Clearly, the conclusion that the ALJ reached on a critical element of churning, that is that Calabro exercised

de facto control over ██████' account is based firmly on the fact that the ALJ believed the testimony of ██████ and found him credible, and disbelieved Calabro and found him to be not credible. This is precisely the type of credibility determination that should be given substantial deference.

A key factor in determining whether control exists is whether the customer lacks the ability to manage the account and routinely follows the recommendations of the registered representative (as opposed to exercising independent judgment). *Mihara*, 619 F.2d at 821. Registered representatives may “exercise *de facto* control where a customer places his trust and faith in a broker and routinely follows his broker’s advice.” *Cruse v. Equitable Sec. of New York, Inc.*, 678 F. Supp. 1023, 1030-31 (S.D.N.Y. 1987) (noting that “factors relevant to the element of control include the discretion given the broker-dealer, the age, education, intelligence, and business and investor experience of the client, the relationship between client and broker, and the reliance placed by the customer on his broker, citing to *Zaretsky v. E.F. Hutton & Co., Inc.*, 509 F. Supp. 68, at 74 (SDNY 1981); see also *In re Mark Gilbert Platt*, Exchange Act Release No. 8275 (Aug. 25, 2003) (in a default judgment, ALJ found registered representative had *de facto* control of the accounts since the unsophisticated customers relied on his recommendations); *Simpson*, 2002 SEC LEXIS 1278, at *53 (*de facto* control shown by numerous unauthorized transactions and customers’ general lack of investment knowledge and sophistication); *In the Matter of Al Rizek*, Admin. Proc. File No. 3-9041, 1999 SEC LEXIS 1585 at * 19 (Aug. 11, 1999) (Commission opinion rejecting respondent appeal of control issue; “Although Rizek’s customers may have been successful businessmen and most of them had some degree of higher education, they were totally lacking in the degree of investor sophistication necessary to understand Rizek’s strategy and unable to make any sort of independent evaluation of that strategy.”); *In the Matter of Joseph J. Barbato*, Admin. Proc. File

No. 3-8575, 1996 SEC LEXIS 3138, at *50-51 (1996) (Although a customer “had some prior investment experience, authorized the transactions in his account, and kept records of his trades, he lacked vital information about the investments he was making ... [and] was unable to make an independent evaluation” of the broker’s recommendations.”).

As noted by the ALJ in the *Rizek* initial decision, a variety of factors come into play when determining the control element with respect to non-discretionary accounts:

Some factors to consider in determining whether or not a broker controlled an investor's account include: the investor's sophistication; the investor's prior securities experience; the trust and confidence the investor has in the broker; whether the broker initiates transactions or whether the investor relies on the recommendations of the broker; the amount of independent research conducted by the investor; and the truth and accuracy of information provided by the broker.

In the Matter of Al Rizek, Admin. Proc. File No. 3-9041, 1998 WL 73209 at *13 (Feb. 24, 1998).

In this case, Calabro exercised *de facto* control over ██████’ non-discretionary account. As the ALJ correctly concluded, ██████ was not a sophisticated investor. [T. 1399-1447 (Williams)] ██████ clearly had no extensive prior investing experience. While he had but one brokerage account prior to his JP Turner account, ██████’ pre-existing account at Smith Barney had been conservatively managed, sparsely traded, and directed by recommendations from his broker for that account. [T. 1402-10 (██████)] ██████ placed great trust and confidence in Calabro during the time that excessive trading was taking place, and believed that Calabro was looking out for his best interest. [T. 1426, 1428-29, 1458-59 (██████)] The evidence overwhelmingly showed that, in ██████’ account, Calabro initiated nearly all the transactions, that ██████ essentially had no input, and that ██████ was relying on his broker’s recommendations when trades were made. [T. 1450-57 (Williams); DOE Ex. 155] And because ██████ was relying so heavily on Calabro, ██████ was not doing any independent

research – indeed, he felt like he lacked the knowledge and experience to do the research necessary to trade in stocks on his own. [T. 1456-57 (██████████)] Regarding the truth and accuracy of the information provided by Calabro, ██████████ knew only what Calabro told him, and he lacked the sophistication or the research skills to analyze. [T. 1450 (██████████)] Indeed, the information that should have been conveyed – the level of commissions being charged and their long-term impact when engaging in active trading – was typically not mentioned at all by Calabro. [T. 1504 ██████████] And finally, the evidence adduced at the hearing showed that, despite the fact that these accounts were technically non-discretionary, Calabro engaged in unauthorized trading in the ██████████’ account. [T. 1451-52 (Williams)] As the Commission has previously found, unauthorized trading in non-discretionary supports a finding of de facto control in the churning context. *Simpson*, 2002 SEC LEXIS 1278, at *53 (“[d]e facto control was shown by the many unauthorized transactions and the customers’ general lack of investment knowledge and sophistication, which left control of the account in the hands of [the respondent]”)

At the hearing, ██████████’ testimony demonstrated that he was an unsophisticated investor who lacked the ability to understand the trading strategies (to the extent there was one) being used, or to make an independent evaluation of that strategy. He had very limited prior experience investing in securities. As evidenced as much by the large investment ██████████ entrusted to Calabro, as by his testimony, he placed great confidence and trust in Calabro. ██████████ testified that he relied on the recommendations of Calabro, who as evidenced by the account statements initiated virtually every trade during the churn period. ██████████ could not recall trades he had even suggested. ██████████ testified he conducted no independent research, and Calabro had to be aware of that from the tenor of the discussion when recommendations were made. And the most important information for ██████████ to consider when making trading

decisions – the risks of active trading – was never imparted by Calabro to him. The unauthorized trades similarly weigh in favor of a finding of control. Thus, based on the factors previously applied in Commission proceedings determining control for purposes of churning, Calabro clearly had *de facto* control over [REDACTED]’ account.

Similarly, the fact that [REDACTED] received account statements and trading confirmations does not negate the *de facto* control exercised by Calabro. Mere receipt of the account statements and confirmation slips does not establish that the customers understood what was happening in their accounts.⁹ [REDACTED] was an unsophisticated securities investor who relied on and trusted his registered representative. *See Schofield v. First Commodity Corp. of Boston*, 793 F.2d 28, 36 (1st Cir. 1986) (investor did not ratify firm’s unauthorized actions or excessive fees by failing to object to them after receiving account statements); *Modern Settings v. Prudential-Bache Sec.*, 936 F.2d 640, 646 (2d Cir. 1991), (“When a customer lacks the skill or experience to interpret confirmation slips, monthly statements or other such documents, courts have generally refused to find they relieve a broker of liability for its misconduct.”) (citing *Karlen v. Friedman & Co.*, 688 F.2d 1193, 1200 (8th Cir. 1982)).

2) The ALJ’s Conclusion That The Trading In [REDACTED]’ Account Was Excessive Was Also Based On Credibility Findings

On the second element of churning involving excessive trading in [REDACTED]’ JP Turner account, Calabro raised arguments before the ALJ that are similar to those he has raised in this appeal. Those arguments include: 1) that the new account forms, options forms, AASQs, AASSs and other papers in the [REDACTED] file supports the conclusion that [REDACTED] was a speculative investor with a risk tolerance of aggressive; 2) that [REDACTED] understood Calabro’s investment

⁹ There was ample evidence showing that JP Turner’s account statements did not reflect the commissions paid by customers, and that the trading confirmations typically required some calculations to determine the commission paid.

strategy was short-term and involved high-risk; 3) that the paper forms in ██████' JP Turner were not blank when he signed them; and 4) that the Division's evidence of turnover and cost equity factor is unreliable. (Initial Decision, pp. 108).

In rejecting each of these arguments, the ALJ wrote:

██████ testified that his risk tolerance was moderate or conservative, that he had limited general investment knowledge, and that his investment objectives were more in line with preservation of capital and capital appreciation than speculation. Tr. 1438-39, 1443-44, 1448. I find ██████' testimony on these points to be credible and supported by the record. For example, the fact that ██████' S&B [Smith Barney] account was managed for fifteen years by the same broker, and stocks were held for an average of ten years, supports ██████ testimony. (Initial Decision, pp. 108-109).

Clearly, the fact that the ALJ found ██████ more credible than he found Calabro on the critical subjects of risk tolerance and investment objectives, had a significant effect on the conclusion that excessive trading occurred during the churn period in ██████' account.

Calabro similarly raised the argument before the ALJ that ██████' post JP Turner, brokerage account at Newbridge Securities¹⁰ had incorrect information about ██████' trading objectives and risk tolerance. On this point, the ALJ specifically noted that ██████ had "consistently and emphatically" testified that both his JP Turner and Newbridge accounts contained inaccurate information about his true risk tolerance and investment objectives.

██████ always insisted that his true investment objectives were capital preservation and capital appreciation, and that his risk tolerance was never greater than moderate. (Initial Decision,

¹⁰ Calabro contends that ██████ post JP Turner account with Newbridge Securities proves him to be a speculative investor. This argument is not persuasive. An account was opened in ██████' name with Newbridge Securities in April 2009. However that account contained incorrect information---including that ██████ was a speculative investor. ██████' testimony was explicit that he did not fill out the application and that when he learned that he had falsely been listed as a speculative investor he adamantly insisted with Newbridge that the information be corrected. [DOE Ex. 216; T. 1403-06, 1411, 1508-1510, 1512, 1549, 1558-59, 1563-1564, 1635]. Clearly, ██████ did not recall the application, did not fill it out himself and did not notice for some time that the small Newbridge account (with a \$15,000 balance) had him listed as a speculative investor. [T. 1558-1559, 1563-1564, 1635]. When he learned the account falsely listed him as a speculative investor, he sent more than one directive to correct the error, with the last directive stating as to speculation: "No, No, No. This is the second time you have been told. This was probably John Quinn's idea in order to save his ___." [DOE 216, T. 1512].

p.108). ██████' minimal trading in that account confirms that he actually had a conservative investment objective for that account. (Initial Decision at 109). The ALJ also noted that ██████ sent directives to Newbridge to correct the error after ██████ learned about that error. In finding that ██████' true investment objectives never included speculation, and that ██████ did not have an aggressive risk tolerance, the ALJ distinctly found ██████ credible and Calabro, not credible. (Initial Decision, p. 108)

Also regarding the churning element of excessive trading in ██████' account, the ALJ distinctly found the testimony of expert Louis Dempsey to be credible and persuasive. (Initial Decision, pp. 109-110). Dempsey opined that from his review of the activity in the ██████ account and the monthly statements revealed that during the period from December 2008 through November 2009, Calabro engaged in trading patterns consistent with churning by executing over 122 sales transactions totaling \$8,588,124.41 and over 149 purchase transactions totaling \$11,015,161.13. These trades resulted in losses in the account of approximately \$1,026,546 and generated commissions and fees to JP Turner of approximately \$297,515. Calabro's aggressive trading in this account resulted in an annualized equity turnover of 8 times on an annualized basis and a cost equity factor of 22.9%. [DOE Ex. 155, pg. 15-16 **The ██████' Account Trading Activity**, ¶[27] All of this is consistent with the findings of the ALJ, at page 109 of the Initial Decision, where he concluded that in the relevant period, the ██████ account had a turnover rate of 8 and a cost equity factor of 22.9%. Without doubt, the ALJ found Dempsey to be credible in his calculations regarding the excessive trading in the ██████ account. Moreover, the ALJ specifically rejected all of Calabro's arguments related to short trading and market volatility to be unpersuasive, noting that "even using Calabro's modified 'short' formula, the turnover rate in ██████' account was 6.6, which is conclusive of

churning for a conservative account, finding his contentions not credible. See Initial Decision, pg. 109.

To underscore the level of trading activity in the accounts managed by Calabro at JP Turner in 2008 and 2009, the Commission should also consider the testimony of the highest ranking JP Turner executive who testified at trial—Michael Bresner.¹¹ Bresner offered executive level insight about Calabro’s trading activity. For example, Bresner was aware that Calabro’s accounts regularly reached Level 4 reviews in the AARS system (the highest level available in the system, coinciding with *the most actively traded accounts* that the AARS recognized) because Bresner personally reviewed many of Calabro’s accounts each quarter. [T. 2879, 2883]. The Executive Vice President at JP Turner was fully aware that Calabro had very active trading accounts in 2008 and 2009, and was also aware that Calabro had been sued in arbitration for churning the account of his client Adcock. [T. 2880-2882]. Bresner, and presumably other executive level management, were also aware that Calabro was a large producer for the firm, in terms of generating commissions. [T. 2883]. For example, in 2008, Bresner and others in management knew that Calabro was near the top of all registered representatives in terms of total revenue for the firm. [T. 2884]. Bresner knew Calabro was a top producing broker for the firm¹² because Calabro was in attendance at all the top producing conferences held by the firm. [T. 2885]. By virtue of Bresner’s position as the highest ranking reviewer of highly actively traded accounts in the AARS system, he distinctly knew Calabro was

¹¹ Although Bresner was charged with failure to supervise accounts managed by Konner and Koutsoubos when those accounts reached Level 4 reviews in the AARS system, Bresner was not charged with a failure to supervise the very actively traded accounts of Calabro.

¹² Bresner identified exhibits at trial which listed the top 50 producers by revenue for JP Turner in 2008 and 2009. [DOE Exs. 94, 95, 96; T. 2885-2895]. Calabro, Konner and Koutsoubos all appeared at various rankings for the top 50 JP Turner registered representatives. [T. 2885-2890]. Calabro was the top firm revenue producer with revenue of \$4,113,085. Konner was included on the list with revenue totaling \$328,837.49. Koutsoubos was included on the list with revenue totaling \$137,035. [DOE Ex. 94, T. 2885-2890].

a registered representative who regularly engaged in active trading. Simply put, Calabro's excessive trading in his clients' JP Turner accounts in 2008 and 2009 was no secret to JP Turner management.

3) Credibility Determinations Relating To Calabro's Scienter In The Churning Of ██████' Account

Finally, as to Calabro's scienter in the churning of ██████'s JP Turner account, the ALJ noted that Calabro had the requisite scienter to churn the account because he engaged in "unauthorized and excessive trading and unilaterally devised and carried out an investment strategy contrary to ██████' investment objectives and risk tolerance, which resulted in a substantial gain for Calabro and a massive loss for ██████." (Initial Decision, p. 110). To reach this conclusion, the ALJ had to credit the testimony of both ██████ and Dempsey, and to reject as not credible the testimony of Calabro. To underscore that finding, the ALJ further stated:

I find ██████' testimony that "Calabro would sometimes exaggerate the results of his trading" credible. Tr. 1472, 1459. To the extent Calabro's testimony is inconsistent with ██████ on these points, I credit ██████; as described above, Calabro's testimony is replete with inconsistencies, changed stories, and general confusion. Calabro was, quite simply, not a believable witness on most critical points. Based on the foregoing, I conclude that Calabro acted intentionally, that is with scienter, and churned ██████' account. (Initial Decision, p. 110).

Establishing that someone has the requisite scienter to churn an account is a very difficult element to prove directly-requiring the finder of fact to look at all of the objective evidence, and to try to understand what the intent inside the head of the violator. In this case, the ALJ weighed documentary evidence, and the relative weight of the testimony of the various witnesses. He ascribed credibility determinations and explained how he arrived at that conclusion. Those determinations are entitled to substantial deference. *See Leslie A. Arouh*, Exchange Act Rel. No. 50889 at n.40, 2004 WL 2964652 (Dec. 20, 2004) ("As we have stated previously, the credibility

determination of an initial fact finder is entitled to considerable weight and deference because it is based on hearing the witnesses' testimony and observing their demeanor"), citing, *Daniel Joseph Alderman*, 52 S.E.C. 366, 368 (1995), *aff'd*, 104 F.3d 285 (9th Cir. 1997); *Jonathan Garrett Ornstein*, 51 S.E.C. 135, 137 (1992).

The specific scienter requirement for churning is met where the registered representative acts to benefit himself by earning commissions, rather than acting for the benefit of his customer. *Donald A. Roche*, 1997 SEC LEXIS 1283, at *12-13, (citing *Mihara*, 619 F.2d at 820-21; *In re Albert Vincent O'Neal*, Exchange Act Release No. 34116, 1994 SEC LEXIS 1639, at *5-6 (May 26, 1994)). In the context of churning, the requisite scienter may be "implicit in the nature of the conduct." *Franks v. Cavanaugh*, 711 F. Supp. 1186, 1191 (S.D.N.Y. 1989 quoting *Armstrong v. McAlpin*, 699 F.2d 79, 91 (2d Cir. 1983)). Scienter also may be established upon a showing of recklessness. *Sharp v. Coopers & Lybrand*, 649 F.2d 175, 193 (3rd Cir. 1981). The scienter element may also be inferred from the commissions charged by the registered representatives. See *In re David Wong*, Exchange Act Release No. 45426 (Feb. 8, 2002); see also *In re Donald A. Roche*, 1997 SEC Lexis 1283 (June 17, 1997)(Commission opinion)(concluding that the fact that client accounts sustained large losses while the registered representative generate substantial commission income can show that the registered representative acted in reckless disregard of his customer's interest and account objectives).

A number of facts in evidence demonstrate Calabro's scienter.¹³ His customer [REDACTED] testimony shows that Calabro engaged in deceit and manipulation with him. Calabro's practice of adding critical investment objective and risk tolerance information to his brokerage account applications either after they were signed by the customers, or giving customers only the last

¹³ In addition to the discussion below, the unauthorized trading in the customers' accounts also supports an inference of scienter. [T. 1451-52 (Williams)]

page to sign so that the objectives were undisclosed, was obviously manipulative and deceitful and applied to all the customers whose accounts Calabro allegedly churned. [T. 630-60 (██████████); 1055-56; 1064-66; 1073-86; 1111-16 (██████████); 1436-44; 1478-85 (██████████)]]

In addition, perhaps the strongest evidence of scienter is the excessive trading itself, and the commissions it generated. *Rizek*, Admin. Proc. File No. 3-9041, 1999 SEC LEXIS 1585 at *19-20 (Aug. 11, 1999) (rejecting defense of good faith belief in active trading strategy and finding “no justification for recommending it to unsophisticated customers who were incapable of making an independent judgment, when he knew that the extremely high risk was directly contrary to the customers’ conservative investment objectives”); *Wong*, Exchange Act Release No. 45426 (Feb. 8, 2002). As evidenced by the very high cost-to-equity rates, turnover ratios and commission levels, Calabro acted with scienter by executing the transactions in ██████████ account for his personal monetary benefit. Calabro knew that ██████████ was an unsophisticated securities investor who relied on him to manage his account and ensure that his investments were in compliance with his true risk tolerance and investment objectives. Instead of honoring those expectations, however, the respondent Calabro recommended hundreds of trades for the purpose of generating additional commissions.

Additionally, Calabro knew, or should have known, that the trading levels in ██████████ account vastly exceeded the “frequency of trades” indicated in associated account documents related to the customer’s account. While ██████████’ March 2009 AASQ listed “Frequency of Trades” at 3-6 per month, Calabro for example executed 13 trades in April 2009, 38 trades in May 2009 and 45 trades in June 2009—the three months *immediately following* ██████████’ *March 2009 AASQ*. [DOE Ex. 45; DOE Ex. 8; T. 1486-90] Nevertheless, Calabro, as the cherner, took advantage of his defrauded customer’s naiveté and loyalty and engaged in a trading that directly conflicted with the actual desires and investment objectives of the customer. Finally, Calabro’s

churning in ██████' account earned Calabro substantial financial gain. Calabro earned \$282,000 in commissions and fees in the twelve month churn period, while his customer ██████' associated losses totaled \$1.3 million.

III. THE ALJ CORRECTLY CONCLUDED THAT CALABRO CHURNED ██████ ACCOUNT, AND THE VOLATILITY OF MARKET CONDITIONS DURING THE CHURN PERIOD DOES NOT ALTER THAT CONCLUSION

Calabro also essentially argues that volatile market conditions during the time ██████' account was churned- December 2008 through November 2009-should somehow have given Calabro a pass on churning. (Calabro Brief, pp. 14-16). Any suggestion that a broker can escape liability on a churning violation because it occurred in a volatile market period is simply irrational, and is not in the interest of the investing public.

In Calabro's brief before the Commission, he again raises the argument that the Division's expert's calculations of turnover and cost-to-equity (or breakeven rates)¹⁴ were based on a faulty methodology because the expert allegedly failed to account for "the 'anomaly' of

¹⁴ Courts have often used two metrics in churning cases when determining whether trading is excessive. One of those metrics is turnover ratio. The turnover ratio in an account measures the number of times during a given period that the securities in an account are replaced by new securities. Although no specific turnover rate is definitive, a rate in excess of six is generally presumed to reflect excessive trading. *Arceneaux v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 767 F.2d 1498, 1502 (11th Cir. 1985); *Mihara*, 619 F.2d at 821; *Franks v. Cavanaugh*, 711 F. Supp. 1186, 1191 (S.D.N.Y. 1989).

The other metric is cost-to-equity ratio, sometimes called a breakeven rate or (as in JP Turner's AARS) return on investment. The cost-to-equity ratio determines the percentage of return on the customer's average net equity needed to pay broker-dealer transactional charges and other expenses or, in other words, the amount of return necessary for the account to break even. A registered representative is presumed to have excessively traded an account when the trading is so extensive that the account requires a 20% cost-to-equity ratio. *See In re Sage Advisory Services*, Exchange Act Release No. 44600, 2001 SEC LEXIS 1482, at *15 (July 27, 2001) (settled) (citing *Rizek*, 1999 SEC LEXIS 1585, at *17); *In re Sandra Simpson*, Exchange Act Release No. 45923, 2002 SEC LEXIS 1278, at *49 (May 14, 2002) (Commission opinion) (Annualized turnover rates of 2.10 to 8.09 and annualized breakeven rates of 11.98% to 54.95% are excessive); *In re Laurie Jones Canady*, Exchange Act Release No. 41250, 1999 SEC LEXIS 669, at *17 (Apr. 5, 1999) (Commission opinion) (Annualized turnover rates ranging between 3.83 and 7.28 and breakeven levels of 8.96% to 27.48% are excessive).

market forces on a ‘short account.’” Calabro’s Brief, pp. 22. Specifically, Calabro claims that the standard, industry-accepted method of calculating turnover ratio is flawed because (assuming purchases are made) the ratio will be slightly higher if the stocks purchased decrease in value rather than staying the same or going up. The change occurs because when the purchased stock goes down in value, it negatively impacts average account equity at month’s end. Calabro further claims that this phenomenon gets worse when one engages in unsuccessful short sales, thus making average account equity go down even further because the trader lost money. Calabro also asserts that the standard, industry-accepted method of calculating breakeven rates is similarly flawed because a declining market and losing on short sales cause account equity to drop, thus causing the cost-to-equity ratio to go up. Id.

These arguments are simple sleight of hand. (They were also soundly rejected by ALJ in the third full paragraph of page 109 of the Initial Decision). Initially, Calabro’s suggestion that fluctuation in account value (whether due to the market declining or transaction losses) is a novel “anomaly” that is so radical that it demands its own turnover and breakeven calculation is absurd. The industry-accepted methods that Dempsey used in this case have, of course, been applied by the Commission in other situations involving declining average account equity; indeed, such events never play out in a vacuum. In addition, even using Calabro’s calculations, the turnover and breakeven rates are still very high – his artificial methods of calculation resulted in hypothetical reductions in turnover in the [REDACTED] account from 8 to 6.6, and a change in the cost equity or breakeven rate from 22.9% to 18%. (T. 3270-3275, 3281-3283) In sum, Calabro’s argument that Dempsey’s methods are flawed and that the Commission should reject his calculations fails. Dempsey used the industry-standard method of calculating turnover and breakeven rates, and Calabro’s situation is not so unique as to warrant special or novel treatment.

During trial, Calabro essentially had Dempsey conduct several unconventional calculations during his cross-examination for his JP Turner clients ██████ and ██████. Dempsey complied with the request, but, as stated, all of the alternative re-calculations yielded turnover ratios or break-even rates that, when annualized, still exceeded presumptive levels for churning. [T. 3284-3288].¹⁵ While Calabro still argues before the Commission for this alternative calculation, he offers no cases in which his alternative calculation has been used. Moreover, Calabro cites no learned treatises or other sources to suggest his theoretical alternative methodology has been subject to peer-review. This void of authority in Calabro's argument can only be because no such cases or learned treatises exist to support his alternative calculation approach. Calabro has no reasonable basis to ask the Commission to reject the turnover ratios and cost-equity calculations offered by the churning expert Dempsey, as to the ██████ account.

At the trial in this case, Dempsey's testimony on redirect examination was unequivocal. The alternative calculations Calabro touts are *completely unconventional in the brokerage industry*, and there is no legal or other basis for the calculations Calabro proposes. [T. 3284-85, 3289]. Dempsey explained that his conventional turnover and break-even methodology set forth in DOE 155 was more appropriate because it effectively averages out end of the month equities. By doing so, the conventional calculation takes into account market fluctuations that occur over a longer period of time. [T. 3285].

There is simply no basis for Calabro's assertion that Dempsey's calculations are based on faulty methodology—Dempsey's methodology for calculating turnover and break-even rates is widely accepted by the industry. To “account for market forces” on a “short account” is not a

¹⁵ Dempsey testified that specifically the turnover in the ██████ account using Calabro's alternative calculation would still have been 6.6% on an annualized basis, which is presumptive of churning. [T. 3285-3286]. Similarly, the alternative calculation for turnover in the ██████ account on an annualized basis would have been 6.72%, also presumptive of churning. [T. 3286-3287].

factor that has any legal or other basis in conducting turnover ratios or break-even calculations—and Calabro cites no authority to support it. In fact, Calabro’s argument fails because under his analysis, calculations would be static—and not based on movement of the market over time.¹⁶ Even after Calabro’s creative but ineffective argument at trial for alternative turnover ratios and break-even calculations, Dempsey insisted that his calculations were done in the conventional methodology used in the industry, and that he stood by his turnover and breakeven calculations as they had been calculated in DOE Ex. 155. [T. 3289].

As a practical matter, Calabro could have subpoenaed and called his own churning expert to testify presumably on his hypothesized alternative turnover ratios and breakeven calculations. Calabro’s failure to do so suggests that no expert has adopted Calabro’s purported methodology. Louis Dempsey’s report, calculations and testimony together comprise the *only evidence of actual turnover ratios and breakeven calculations* that are before the Commission. [DOE Ex. 155]. Because his methods of calculating breakeven ratios and turnover rates are ones commonly used in the brokerage industry, they are reliable evidence before the Commission. The churning expert’s testimony was unaltered and his calculations in DOE Ex. 155 were unaffected by Calabro’s questions on cross-examination. The turnover and break-even calculations in this case are overwhelmingly excessive and indicative of churning—not only as to [REDACTED]—but to [REDACTED] and [REDACTED] as well.

¹⁶ Even if an expert considered market conditions in doing turnover and breakeven calculations, that analysis is essentially a static calculation, and not one based on movement in the account over time. As a short account inflates the term over cost equity, the reason that Dempsey and other regulatory professionals calculate turnover ratios and break-even rates over time the way they do, is that it tends to smooth out the calculations giving no moment in time more persuasive authority than another. As a practical matter, the longer period of time that is looked at, the better it is because the calculations will smooth out over time. Essentially, that is precisely the reason that turnover and break-even rates are calculated on an annualized basis.

██████████ placed his liquid retirement nest-egg with Calabro for Calabro's management of the trading in his account. There is little doubt but that Calabro placed ██████████ in an extremely risky trading program that involved shorting in various stocks Calabro recommended. Calabro has admitted that he knew he was engaging in very risky, complicated trading activity in the ██████████ account and that he never really advised any of his clients that they had to earn 25% or 30% or more in their accounts just to reach the breakeven point, before each of them could actually begin to earn a trading profit in their brokerage accounts. [T. 4255, 4301-4303]. Calabro argues much about market volatility in 2008 and 2009 and uses that volatility to defend the fact that he placed a largely inexperienced stock investor in an extremely risky shorting strategy without insuring that ██████████ had an understanding of the potential losses he could suffer in his account using Calabro's shorting strategy. Notably however, the Commission should consider that even after the stock market largely corrected itself in March 2009, Calabro failed to alter his shorting strategy in the ██████████ account. As Calabro was admittedly aware of the riskiness of his shorting strategy, his failure to alter his shorting strategy for ██████████ as the market improved in 2009 amounted to willful and reckless disregard for the interests of his clients. [T. 4213-4214, 4245, 4255, 4274, 4302-4303]. As the ALJ correctly concluded, Calabro has in fact churned the account of ██████████.

Calabro also argues that Dempsey's expert opinion was based upon the conclusion that ██████████ had a conservative investment objective. As Calabro would have the Commission believe that he has disproved conservative investment objectives for ██████████, he contends that the trading in ██████████' account was somehow appropriate—even authorized, and that Dempsey's opinion is faulty because he assumed a conservative investment objective for ██████████. Dempsey's opinion that the trading activity in the accounts was consistent with churning, and that the brokers' control of the direction of the trading activity in their respective

accounts, was not however dependent upon each customer's investment objectives. Dempsey stated that his churning opinion and calculations were not based upon what the customer's investment objectives actually were. [T. 3170-3172, 3192, 3198, 3200, 3210, 3292-3293]. Moreover, Dempsey stated that it is essential for a client to fully know and understand what he is getting into with actively traded accounts. Dempsey further stated that "most customers they found do not have the time or the sophistication to be able to monitor active trading in an account. That is one of the things you would assess." [T. 3294-3295]. Dempsey stated that the thresholds for churning (with Turnover of 6 being presumptive of churning) *do not actually change* from a conservative investor along the spectrum to a speculative investor. [T. 3297]. Dempsey's conclusion that the trading activity is consistent with churning for the [REDACTED] account, is simply unaffected by [REDACTED]' investment objectives.

IV. CALABRO'S CAREER, AND THE APPROPRIATENESS OF THE ALJ'S ORDERED SANCTIONS FOR CALABRO'S CHURNING OF [REDACTED]' ACCOUNT

Throughout his initial appellate brief, Calabro suggests that he has been hurt enough by the filing of this enforcement proceeding and that the sanctions against him by the ALJ should not be enforced, even if the Commission concludes, as did the ALJ, that Calabro churned [REDACTED]' JP Turner account. For example, Calabro contends erroneously that: 1) he has voluntarily "relinquished" his career as a registered representative, and he should not therefore be barred from association with a broker or dealer; 2) that the FINRA arbitration settlement paid to [REDACTED] after the trial in this matter satisfies the victim account holder, and therefore the monetary obligations order by the ALJ should be vacated; and 3) that even if the judgment against him is upheld by the Commission, Calabro has an inability to pay the amounts ordered against him. For the reasons set forth below, each of these equitable arguments is without merit and should be rejected by the Commission.

A. Calabro Has Not “Relinquished” His Career As a Registered Broker In Any Meaningful Way

In his brief, Calabro suggests that he is no longer in the industry.¹⁷ Even if it is true that he is no longer a broker, Calabro’s conduct in this case as established by the trial record and found by the ALJ was egregious and resulted in swift and substantial losses in ██████████’ JP Turner account. It should be noted that at the hearing in this matter in early 2013, Calabro was then still actively involved as a registered representative with National Securities Corporation, having gone there after he left JP Turner. (T. 104-105)

Moreover, in a highly improper move, Calabro has attempted to support his contention that he has left the securities industry by attaching post-trial “evidence” to his brief, *after* the evidentiary record was finalized and approved by the ALJ in this case. Exhibit 1, attached to his brief, is Calabro’s “BrokerCheck Report” from FINRA, which he caused to be downloaded and printed on or about March 4, 2014. Calabro would have the Commission infer, among other things, that this report supports his contention that he is no longer in the brokerage industry. However, to the contrary, the proffered report only serves to cloud the issue.

For instance, in the “Registration History” section of the BrokerCheck Report on page one of the report, it indicates that Calabro was registered with National Securities Corporation from January 2011 through December 2013, suggesting he is no longer affiliated with that firm. But elsewhere in the report, on Calabro’s “Employment History,” the report indicates that his *employment* with National Securities Corporation is from “01/2011 – Present.” (See p. 4, Ex. 1 to Calabro Brief). This differentiation suggests that while Calabro’s securities license registration is no longer with National Securities, he remains in some capacity, employed by that

¹⁷ In the Introduction to his brief, Calabro states, in a less than clear manner, “. . . Calabro has relinquish (sic) his career as a registered broker.” On page 29 of his brief, he states in past tense that Calabro “has now left the brokerage industry.”

brokerage house. The Division respectfully submits that if this scenario is true, as set forth in Calabro's recent "BrokerCheck Report,"¹⁸ that Calabro is probably still in the "industry" in some capacity.

Moreover, from an enforcement standpoint, the Commission cannot reasonably allow Ralph Calabro to simply assert that he has "relinquished" his career, and thereby escape being barred for his conduct at JP Turner. The ALJ properly ordered that Calabro cease and desist from committing fraudulent acts, and barred him from the industry. He was also ordered to disgorge \$282,000 in commissions he earned from his churning in [REDACTED]' account, plus prejudgment interest thereon, and was further ordered to pay a civil penalty of \$150,000. Those sanctions are fully supported by the evidence adduced at trial, and by the law applied in this case by the ALJ. Calabro's suggestion of relinquishment of his career is likely not the case, and would be inadequate to address his churning conduct in [REDACTED]' account.

B. Calabro's Request To Vacate The Monetary Obligation Ordered Against Him In The Initial Decision Has No Merit

Calabro contends that even if the Commission upholds the ALJ's Initial Decision and concludes that he churned [REDACTED]' JP Turner account, that the Commission should eliminate all monetary components of the decision. Calabro reasons that after the hearing in this matter [REDACTED] entered into a private settlement of his claims and that together with [REDACTED] (another former JP Turner client of Calabro's) whereby the two of the former account holders received \$2,500,000. For two reasons, this settlement should have no effect on the

¹⁸ In addition, the "BrokerCheck Report" dated 3/4/2014 also reinforces that Calabro is a recidivist churning violator, with one regulatory event (this case), and seven customer disputes of which two are pending and five are final. (See pp. 6-7, Ex. 1 to Calabro's Brief) Fully, each of the customer complaints listed in this report, save one, include allegations of churning and unauthorized trading and/or unsuitability. (See pp. 15-24, Ex. 1 to Calabro's Brief) Interestingly, page 23 of the "BrokerCheck Report," reveals that the most recent customer complaint against Calabro was received on December 26, 2013, and indicates that the allegations of churning, unauthorized trading and unsuitability in that complaint were received by Calabro at a time *nearly one year after the trial* in this case, and at a time when Calabro was employed by National Securities Corporation.

disgorgement, prejudgment interest and civil penalty ordered by the ALJ against Calabro. First, the FINRA settlement was paid *only* by JP Turner, and *not* by Calabro. A simple review of the settlement reference of the relevant case at page 17 of Calabro's recent "BrokerCheck Report" indicates that the "Individual Contribution Amount" of the settlement, attributable to Calabro, was *zero*. Secondly, the amount paid by JP Turner to ██████ in that settlement relates only to *losses* that ██████ suffered in his JP Turner account by the hand of Calabro, and does not cover the *commissions* that Calabro personally pocketed from his churning of ██████' account. The amount of disgorgement that the ALJ ordered Calabro to pay, on the other hand, is related only to that portion of the *commissions* paid by ██████ that went into Calabro's pocket or the amount by which Calabro personally benefited from his fraud. (Initial Decision, pp. 76, 121). The ordered disgorgement does not relate in any manner to the trading losses in ██████' account. As the ALJ ordered Calabro to divest himself of ill-gotten gains that he got from commissions he was paid on his own illegal trading in that account, the ALJ's disgorgement order is not duplicative of any other order or settlement and should be affirmed.

As to the \$150,000 civil penalty that the ALJ ordered against Calabro, the Commission should note that this component of the ordered monetary relief is the *only* monetary penalty imposed against Calabro. As disgorgement and the prejudgment interest are designed simply to deprive Calabro of his ill-gotten gain, without the civil penalty ordered by the ALJ, Calabro would escape with no serious repercussions from his churning fraud. In supporting his ordered relief, the ALJ noted:

As to Calabro, Konner and Koutsoubos, the Steadman factors all weigh in favor of a heavy sanction. The actions of Calabro, Konner and Koutsoubos were egregious and recurrent. They recklessly disregarded their customers' conservative investment objectives and risk tolerances and pursued an active trading strategy generating thousands of dollars in commissions. Calabro unilaterally devised and executed an investment strategy contrary to ██████ investment objectives. . . Calabro's, Konner's and Koutsoubos' violations

spanned months and involved hundreds of trades. As noted above, Calabro acted with scienter, Konner with a high degree of scienter, and Koutsoubos with the highest degree of scienter. Calabro, Konner and Koutsoubos have failed to recognize the wrongful nature of their actions and none of them have made any assurances against future violations. In fact, they insist that no violations occurred. All three continue to work in the securities industry today, so their profession presents opportunities to violate the securities laws again.

(Initial Decision, p. 119).

The ALJ further stated that “Calabro, Konner and Koutsoubos clearly have no business associating with the securities industry in any capacity...” (Initial Decision, p. 120). Given these unequivocal conclusions as to, *inter alia*, Calabro, \$150,000 as a civil penalty against him is quite reasonable, but could actually be justified at a substantially higher amount. All monetary components ordered by the ALJ against Calabro should be kept at least at those respective levels ordered, although should the Commission wish, civil penalties could rationally be significantly increased beyond those amounts ordered by the ALJ.

C. Calabro’s Unsubstantiated Claim Of Inability To Pay

Calabro contends on page seven of his brief that he is “financially unable to pay any level of disgorgement or penalty.” This contention should be disregarded because: 1) it is not supported by the record in this case; 2) Calabro was the highest paid representative at JP Turner during his churn years with income in 2008 and 2009 exceeding \$3,000,000; and 3) Calabro has never filed a sworn statement of financial condition with the Commission despite having been directed to do so by the ALJ. Calabro raises his alleged inability to pay almost as an aside to his argument that the monetary obligations in the Initial Decision should be overturned, even if the Commission concludes that Calabro churned [REDACTED] account.

The ALJ directed that the Respondents in this case should take heed to file and/or update sworn financial disclosure statements. (Initial Decision, p. 125). Pursuant to 17 C.F.R. § 210.410(c) the ALJ instructed the Respondents that “[a]ny person who files a petition for review

of an initial decision that asserts the person's inability to pay either disgorgement, interest or a penalty shall file with the opening brief a sworn financial disclosure statement containing the information specified in Rule 630(b)." However, Respondent Calabro has *never filed* a sworn financial disclosure statement with the Commission, and has certainly never served the Division of Enforcement with any such filing—yet contends he has an inability to pay the judgment. As there is significant evidence in the record that Calabro made, at least, hundreds of thousands of dollars in commissions at JP Turner, at least in each of his last several years at the firm and was the firm's leading revenue producer in the millions of dollars for a period of years, Calabro should be required to fully establish under oath any claimed inability to pay. Since he has not satisfied that evidentiary burden, the Commission should presume that Calabro has a true ability to pay and the judgment against him should be affirmed.

V. CONCLUSION

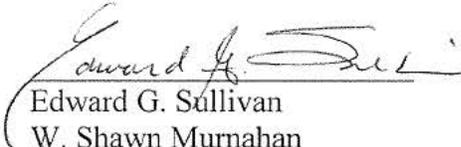
Calabro violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, when he as a registered representative at JP Turner, churned the brokerage account of [REDACTED]. In the interests of protecting the investing public, he should be ordered to cease and desist from further fraudulent activities and be barred from the industry, be ordered to disgorge all commissions he personally retained from the trading in [REDACTED]' account during the respective churn period, along with prejudgment interest thereon. Calabro should also be ordered to pay civil penalties, at least equal to the amount of disgorgement proved against him in [REDACTED]' JP Turner account.

In his Initial Decision, the ALJ made extensive credibility determinations that explain the rationale for his decision. [REDACTED] was deemed to be highly credible, while Calabro was found to have provided confusing and inconsistent testimony and demeanor during the hearing in this matter. Moreover, the ALJ obviously credited the testimony of the Division's churn expert

Louis Dempsey, and fully adopted his calculations on both the turnover rate and cost-to-equity ratio in ██████ JP Turner account. As the Commission has consistently held, credibility determinations made by the finder of fact who observed the demeanor and character of the witnesses as they testified, are entitled to significant deference, and should be upheld. The ALJ's Initial Decision as to the conclusion that Calabro controlled ██████ JP Turner account, and actively traded in that account with scienter, for the primary purpose of lining Calabro's own pockets should be affirmed in all respects.

Respectfully submitted, this 3rd day of April, 2014.

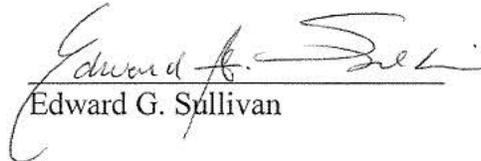
Respectfully submitted,


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CERTIFICATE OF COMPLIANCE WITH SEC'S RULE OF PRACTICE 450(c)

I hereby certify that this brief complies with the length limitation set forth in SEC Rule 450(c). According to the word processing system used to prepare this document, the brief contains 13,600 words.


Edward G. Sullivan